

J. SUBSTANTIATION AND DISCLOSURE RULES OF OBRA '93

**by
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1. Introduction

OBRA '93 imposes two new requirements concerning charitable contributions. These requirements are referred to as the "substantiation" and "disclosure" requirements. The revenue they are expected to raise is intended to offset the revenue loss of the OBRA '93 repeal of the AMT rules on capital gain property. This article discusses the substantiation and disclosure requirements.

2. The Substantiation Requirement

IRC 170(f)(8) provides that for contributions made on or after January 1, 1994, no deduction will be allowed under IRC 170 for any charitable contribution of \$250 or more unless the donor has a "contemporaneous written acknowledgment" from the donee organization. The acknowledgment must contain three items:

- (1) The amount of any cash contribution, or, in the case of noncash contributions, a description of the property,
- (2) A statement of whether or not the donee organization provided any goods or services to the donor in consideration for the contribution, and
- (3) If any goods or services were so provided, a description and good faith estimate of the fair market value of the goods or services.

If the goods and services consist solely of "intangible religious benefits," the acknowledgment need only state this fact, and need not describe or value the benefits. Intangible religious benefits are benefits which are provided by an organization organized exclusively for religious purposes and which generally are not sold in a commercial transaction outside the donative context. Examples of intangible religious benefits include admission to a religious ceremony and de minimis tangible benefits incidental to a religious ceremony, such as wine. Benefits that are not intangible religious benefits include tuition for education leading to a recognized degree, travel services, and consumer goods.

The acknowledgment should be retained by the donor, not attached to the donor's return. Although Congress authorized the Secretary to prescribe rules for donee reporting which would be in lieu of donor recordkeeping, no such rules have been prescribed. Accordingly, donee reporting is not a substitute for donor recordkeeping. A donee organization that knowingly provides a false acknowledgment may be subject to a penalty under IRC 6701 for aiding and abetting an understatement of tax liability.

The acknowledgment must be "contemporaneous." This means the acknowledgment must be received by the earlier of the date the donor actually files the donor's tax return for the year of the contribution, and the due date (including extensions) of the return.

The acknowledgment need not be in any particular form. Letters, postcards, or computer-generated forms are acceptable. The acknowledgment does not have to include the donor's social security number or tax identification number. The acknowledgment may be provided for each contribution of \$250 or more or may be provided in a periodic statement, for example, an annual summary.

For purposes of the \$250 threshold, separate contributions of less than \$250 will not be aggregated. Although the Secretary is authorized to prescribe anti-abuse rules to prevent avoidance of the substantiation requirement by writing multiple checks on the same date, no such rules have been prescribed.

Temporary regulations have been prescribed (section 1.170A-13T (T.D. 8544)) that provide additional guidance. Goods and services that have insubstantial value under the guidelines provided in Revenue Procedures 90-12, 1990-1 C.B. 471, and 92-49, 1992-1 C.B. 987 (and any successor documents) need not be taken into account for purposes of the substantiation requirement.

Under the temporary regulations, a contribution of \$250 or more made by payroll deduction, i.e., a single paycheck deduction of \$250 or more, can be substantiated with a combination of two documents: 1) a pay stub, Form W-2, or other document from the employer indicating the amount withheld by the employer, and 2) a pledge card or other document from the donee organization that includes a statement that the organization does not provide goods or services in consideration for contributions made by payroll deduction. The temporary regulations also provide that substantiation may be provided by a donee organization even if that organization pursuant to the donor's instructions

distributes the contribution to another donee organization. This last provision does not apply, however, if the distributee organization provides goods or services to the donor as part of a transaction structured to avoid the substantiation requirement.

3. The Disclosure Requirement

For "quid pro quo contributions" over \$75 made on or after January 1, 1994, IRC 6115 provides that donee organizations must provide certain written statements to donors in connection with the solicitation or receipt of the contributions. A quid pro quo contribution is a payment made partly as a contribution and partly in consideration for goods or services provided to the donor by the donee organization. Note that the over \$75 threshold is determined on the amount of the "payment," not on the amount of the contribution element of the payment. Thus, for example, a payment of \$100 in exchange for a dinner worth \$40 is a quid pro quo contribution, even though the amount of the contribution (\$60) is \$75 or less. Separate payments will not be aggregated for purposes of the over \$75 threshold. As in the case of the substantiation requirement, the Secretary is authorized to prescribe anti-abuse rules to prevent the avoidance of the disclosure requirement by writing multiple checks for the same transaction, but no such rules have been prescribed.

The written statement must: 1) inform the donor that the amount of the contribution that is deductible for federal income tax purposes is limited to the excess of the amount of any money and the value of any property other than money contributed by the donor over the value of the goods or services provided by the donee organization, and 2) contain a good faith estimate of the fair market value of the goods and services. The written statement must be made in a manner that is reasonably likely to come to the attention of the donor. For example, a disclosure of the required information in small print set forth within a larger document might not meet the requirement.

The disclosure requirement does not apply if the goods or services consist solely of either benefits of insubstantial value or intangible religious benefits. These benefits are defined in the previous section on the substantiation requirement.

IRC 6714 imposes a \$10 penalty on donee organizations for each contribution for which the disclosure requirement is violated. Violations include the failure to provide a statement and the provision of an incomplete or inaccurate

statement. The total penalty for a particular fundraising event may not exceed \$5,000. If it is shown that the violation was due to reasonable cause, no penalty will be imposed.

4. Q's and A's

The following examples will hopefully provide some guidance on other applications of the new rules.

Question 1 In 1995, taxpayer X presented Y Charity with a contribution in the form of a check in the amount of \$1,000 for which X neglected to claim a charitable deduction on his Form 1040 for 1995, which he filed on April 15, 1996, because X did not get a receipt from the organization until July 15, 1996. In 1997, X filed an amended return for 1995. Will the 1996 receipt obtained by the taxpayer satisfy the substantiation requirement since it was obtained prior to the date of filing the amended return?

Answer Section 170(f)(8) requires obtaining the acknowledgement by the due date (including extensions) of a return. Unlike the Service's granting of an extension to file, the Service's acceptance of amended returns for a tax year after the due date does not require the Service to recognize the section 170(f)(8) statement obtained after the due date as being timely. In fact, such a recognition would be contrary to the statute.

Question 2 A common question concerns the treatment of raffles, lotteries etc. under the quid pro quo disclosure provisions. The purchase price for a ticket is \$85, including the cost of a dinner and entertainment. The dinner is valued at \$25.00 and the entertainment is estimated at an additional \$20.00. Additionally, the ticket entitles the bearer to a chance at a drawing for a car valued at \$22,000. Does the quid pro quo computation disclosure by the charity have to include the value of the donor's chance at winning a \$22,000 car? What amount should be disclosed by the charity as being deductible to the ticket purchaser?

Answer The amount that may be deducted by the purchaser of such a

ticket is zero because the purchaser acquires something of value as the result of his purchase -- the opportunity to win a prize in addition to the value of the dinner and the entertainment provided by the organization. This quid pro quo embraces the entire purchase price of \$85, notwithstanding that the meal and entertainment components total only \$45.00. There is no authority to make an actuarial computation of win probabilities and prize cost to assign a value to the service or opportunity. Under Rev. Rul. 83-130, 1983-2 C.B. 148 and Goldman v. Commissioner, 46 T.C. 136 (1966), aff'd., 388 F. 2d 476 (6th Cir. 1967), the entire price of the raffle ticket is construed as a payment for goods or services. Thus, it is immaterial how much, if anything, in excess of the value of the meal and entertainment may have been paid. The purchaser may not deduct any of the purchase price.

Question 3 The law states that it is the responsibility of the donor to secure the substantiation from the charity regarding any contributions of cash or property of \$250 or more. The law goes on to state that if goods or services are provided by the charity in consideration for the contribution, the substantiation document must include a good faith estimate of the value of these goods or services. Presumably, as a \$250 or more contribution, the responsibility for obtaining the documentation is on the donor. However, the law pertaining to disclosure of \$75+ quid pro quo contributions, stipulates that the charity receiving such contribution is obligated to furnish a statement. Does this mean that if the quid pro quo donation is \$250 or more, the charity is no longer obliged to furnish a statement?

Answer No. The \$250 rule pertains only to the requirement of the **donor** to document his or her contribution by obtaining the stipulated information. The \$75 rule relates only to the requirement of the **charity** to provide a breakdown of the value of the component parts of the quid pro quo contribution. The charity's disclosure for the quid pro quo contribution does not have to be individualized in the form of a "receipt" issued to each donor. It simply has to inform donor(s), whether in an individualized or a generic format, that the item (or service/event) made available to each donor/purchaser will

carry a value of \$x and a charitable donation component of \$y. For example, a flyer advising purchasers of \$75 tickets to a circus that the tickets have a value of \$45 and that the remaining \$30 cost of a ticket will thus be deductible to the donor as a charitable contribution will not suffice to substantiate a \$300 deduction claimed by the purchaser of a block of ten tickets. That person will have to secure an acknowledgement from the charity that the \$750 check received made out to the charity represents payment for ten tickets valued at \$450, of which \$300 represents a charitable contribution. The flyer sent to promote ticket sales will not suffice for purposes of substantiating that patron's claimed charitable deduction of \$300.

Question 4 What is the proper tax treatment of a donor who has purchased from a charity at a premium a subscription series ticket to an entire run of performances? If the donor does not attend, but gives no advance indication of this intention, is there a mechanism through which he or she can take the entire amount paid or value of the ticket as a charitable deduction?

Answer The determining factor is not whether or not the donor has an intention of exercising the right to admission but whether or not the tickets are **accepted** by the donor. If the ticket holder wants to support the charity and forego the right of admission, he or she can simply pay the charity the face value of the ticket and refuse to accept it or the admission entitlement. The charity might consider advising any such persons in advance that it is their right to refuse the tickets and claim the entire amount of payment (or entitlement). The donor who earns the right of admission through giving a prescribed dollar amount, rather than by outright purchase of the ticket, is also entitled to deduct the full amount of his or her payment if he or she relinquishes the prerogative of attending the events. This position was set forth in Example 3 of Rev. Rul. 67-246, 1967-2 C.B. 104, 108, and is still valid.

Question 5 X wrote a check to Y Charity in the sum of \$500. X notes on the check "donation", but does not receive a receipt from Y Charity. X takes a charitable deduction for the amount on his

Form 1040. Is X entitled to the deduction claimed?

Answer No, the deduction is not allowed. The check alone is not sufficient substantiation of the contribution.

Question 6 The Service grants X, an individual whose tax year ends December 31, 1995 and who normally must file by April 15, 1996, a three-month extension to file a Form 1040. X's extended filing date is July 15, 1996. On November 15, 1995, X issued a check for \$500 to the Y Medical Research Foundation as a charitable contribution. X filed a 1040 on June 15, 1996 and, on the same date, obtained a substantiation notice from Y Foundation. **(a)** Is this a "contemporaneous" substantiation? **(b)** If the substantiation statement was obtained on June 16, 1996, would this meet the contemporaneous standard?

Answer The answer to **(a)** is yes. The answer to **(b)** is no. The rule stipulates that the controlling date is the earlier of the date the return was filed or the due date (including extensions) of the return.

Question 7 X donates ten old suits and ten of his used shirts to Y Charity, which resells them at its thrift store. X had left these items on his doorstep, whereupon Y Charity had picked them up and left a receipt stating the number and nature of the items collected and that nothing was provided to the taxpayer in return for the donated goods. Is the substantiation requirement met?

Answer Yes. The receipt properly describes the property donated, and it states whether or not Y Charity provided any goods or services in consideration, in whole or in part, for the property donated. It is important to remember that the quid pro quo aspect has to be addressed in the substantiation document one way or the other; that is, if no goods or services were furnished to the donor, then this fact must be noted. Also note that Y is not remiss in failing to include a dollar amount since the charity has no obligation to place a value on the donation.

Question 8 The same charity that received the box of clothing noted in

Question #7, leaves the donor a receipt which consists entirely of the following statement:

Thank you for your kind donation. We intend to use the proceeds of any sale of the property to provide disaster relief to the victims of the recent flood in Tasmania. Any unsold items will be furnished directly to these victims for their use. Your contribution will assist us in our mission of demonstrating to the unfortunate victims of disasters throughout the world that Americans are a generous and caring people. You might note your estimated value of the contributed goods on the line at the bottom of this receipt.

Is the substantiation requirement met?

Answer No. The notice fails to provide a description of the contributed property. It also neglects to mention whether any goods or services were furnished to the donor in return.

Question 9 Z, a public TV channel, provides contributors with an autographed baseball with a fair market value of \$200, in return for a "contribution" of \$250. Must Z provide a statement under section 6115?

Answer Yes, since each payment is over \$75, the charity must inform its donors that only \$50 is deductible for income tax purposes.

Question 10 A private foundation turns over \$5,000 to the Tinseltown Opera. These are not earmarked funds. The PF shows this expense as a qualified distribution on its form 990 PF (i.e., NOT a charitable contribution). Are substantiation and disclosure notices required?

Answer This is not a charitable contribution for purposes of section 170. The PF is not entitled to, nor will it, take a charitable contribution deduction for the gift.

5. Conclusion

It is important to note that, although the new requirements are intended to

improve compliance and facilitate enforcement, they are not intended to supplant the existing substantiation requirements. These are set out in section 1.170A-13 of the Income Tax Regulations. These regulations include the recordkeeping requirements for cash and noncash contributions. In addition, these regulations provide the special rules for noncash contributions over \$500 and noncash contributions over \$5,000 (Form 8283, Noncash Charitable Contributions, and the qualified appraisal rules). Finally, it is important to note that several important issues remain unresolved, and it is anticipated that future guidance will be issued.